No. 91-194

(250)

IN THE
Supreme Court of the United States

OCTOBER TERM, 1991

QUILL CORPORATION,
Petitioner,
v.

STATE OF NORTH DAKOTA,
by and through its Tax Commissioner,
HEIDI HEITKAMP,
Respondent.

On Writ of Certiorari to the Supreme Court of North Dakota

BRIEF AMICUS CURIAE FOR THE STATE OF NEW JERSEY SUPPORTING RESPONDENT

ROBERT J. DEL TUFO
Attorney General of New Jersey
SARAH T. DARROW *
Deputy Attorney General
JOSEPH L. WANNOTTI
Assistant Attorney General
R.J. Hughes Justice Complex
C.N. 112
Trenton, NJ 08625
(609) 633-8455

RICHARD G. TARANTO
JOEL I. KLEIN
KLEIN, FARR, SMITH & TARANTO
2550 M Street, N.W.
Washington, D.C. 20037
(202) 775-0184
* *Counsel of Record*

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

TABLE OF CONTENTS

TABLE OF CONTENTS—Continued

TABLE OF AUTHORITIES

TABLE OF AUTHORITIES—Continued

IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

No. 91-194

QUILL CORPORATION,

Petitioner,

v.

STATE OF NORTH DAKOTA,
by and through its Tax Commissioner,
HEIDI HEITKAMP,

Respondent.

On Writ of Certiorari to the Supreme Court of North Dakota

BRIEF AMICUS CURIAE FOR THE STATE OF NEW JERSEY SUPPORTING RESPONDENT

INTEREST OF AMICUS

The State of New Jersey, like respondent the State of North Dakota, imposes a sales and use tax on retail sales and tangible property, payable by New Jersey customers and collectible by vendors. Under the New Jersey statute, the term "vendor" is defined as: "A person who solicits business either by employees, independent contractors, agents or other representatives or by distribution of catalogs or other advertising matter and by reason thereof makes sales to persons within the State of tangible personal property or services, the use of which is taxed by this act." N.J.S.A. 54:32B-2(i)(c). Despite this provision, numerous vendors, relying on the decision in *Na-*

tional Bellas Hess, Inc. v. Department of Revenue, 386 U.S. 753 (1967), promote and sell their goods in New Jersey—through the use of direct mail catalogs, telephones, television, and computers—but refuse to collect the requisite taxes. The New Jersey Division of Taxation estimates that in 1990 such direct-marketing sales to New Jersey residents and businesses amounted to approximately $4.34 billion. As a result, New Jersey lost approximately $141 million in tax revenue for that year.

These direct marketers, while refusing to collect the applicable state taxes, nevertheless derive substantial benefits from the organized markets that the State makes available to them. In addition, the flood of direct mail solicitations and glossy catalogs that such vendors pour into the State imposes enormous governmental costs, both directly in terms of waste disposal programs and derivatively in terms of environmental burdens. For these reasons, the State of New Jersey has a direct and immediate interest in the outcome of this litigation. In particular, New Jersey requests that *National Bellas Hess* be overruled so that companies like petitioner can be made to collect and remit their fair share of the taxes necessary to support the benefits that they derive from, and the costs that they impose on, the State.

SUMMARY OF ARGUMENT

This Court's decision in *National Bellas Hess, Inc. v. Department of Revenue*, 386 U.S. 753 (1967), should be overruled. To begin with, it rests on two legal propositions that are inconsistent with constitutional doctrine as it has been clarified since 1967. First, *National Bellas Hess* relies on the formalistic notion that so-called "exclusively" interstate commerce is immune from state taxation, but that notion was explicitly repudiated by this Court in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977). Second, *National Bellas Hess* also relies on the notion that some physical presence in a State is an essential precondition to the State's exercise of jurisdiction over a person, but that notion—which even in 1967 was contrary to due process case law (not cited by the Court in its opinion in *National Bellas Hess*), *see McGee v. International Life Ins. Co.*, 355 U.S. 220, 222, 223-24 (1957); *International Shoe Co. v. Washington*, 326 U.S. 310, 321 (1945)—has likewise now explicitly been laid to rest. *Burger King Corp. v. Rudzewicz*, 471 U.S. 462, 476 (1985). Both doctrinal developments turn away from the rigid formal lines reflected in *National Bellas Hess* toward a more practical focus on current economic realities. *See Complete Auto*, 430 U.S. at 279; *Burger King*, 471 U.S. at 476.

Such a practical focus makes clear that not only the doctrinal underpinnings but also the critical factual assumptions of the majority opinion in *National Bellas Hess* are today insupportable, both factually and as legal grounds for denying state taxing authority over out-of-state direct marketers. First, the idea that States do not accord such marketers protections and services that benefit their businesses (386 U.S. at 757, 760) simply does not fit the facts: state governments provide or protect the essential infrastructure that makes possible the successful, continuing completion of marketers' transactions—*e.g.*, the education and economies that create able consumers; the roads, telephone networks, cable television networks, and other means of communication through which the goods are advertised, sales solicited, orders placed, credit checked, bills sent and paid, and goods delivered; insurance, police, and fire services that protect homes and buildings where goods are used or stored; the banking systems that make possible the ubiquitous use of credit cards; the waste services that enable consumers to dispose of the millions of catalogs marketers send out each year; and the legal institutions that structure and enforce the terms of the commercial transactions. Second, the idea in *National Bellas Hess* that the administrative burdens on marketers justify tax immunity (386 U.S. at 760) is likewise fundamentally wrong. For one thing, the costs of compliance, like the rate of the tax, are

not properly relevant to the constitutional analysis of taxing authority at all under the approach of *Complete Auto*. And, in any event, with the advent of powerful, inexpensive computers, the costs of compliance with state tax laws are now relatively insubstantial.

The problem with *National Bellas Hess* is not simply that its foundations have been rendered clearly anomalous by legal and factual developments since 1967. The decision affirmatively undermines important constitutional values protecting both States and businesses. First, because of the tremendous growth of direct marketing in the past two decades, *National Bellas Hess* removes from the States' tax base an ever-growing share of the nation's commercial activity, depriving States of approximately $2 billion annually. The effect of thus immunizing a $180 billion-a-year industry from *any* State's sales and use tax —placing the industry in a kind of no-state's land within the national economy—is directly to threaten States' constitutionally rooted authority to ensure that *all* businesses that benefit from state services pay their way. Second, in-state businesses are likewise harmed by the tax immunity conferred by *National Bellas Hess*: they not only suffer a direct disadvantage in competing for customers (who can buy goods tax free from the out-of-state firms) but must also pay higher in-state taxes to make up for the diminishing revenue base available to the States. This sort of discrimination between in-state and out-of-state commerce, effectively compelled by *National Bellas Hess*, turns the commerce clause antidiscrimination principle on its head.

Petitioner and its amici have not advanced any good reason for preserving the erroneous, unfair, and outmoded rule laid down in *National Bellas Hess*. In particular, there is no substantial claim to reliance on this discriminatory, often-questioned decision, which was rendered in an area of law where evolution and overruling have long been common. Moreover, concerns about determining

which direct marketers must comply with tax obligations are both insignificant and, in any event, plainly insufficient to justify retention of the rigid rule immunizing even large companies like Quill from state tax obligations. Finally, the issue of whether any overruling of *National Bellas Hess* should be retroactive is separate from the question presented here and should be left for another day.

ARGUMENT

NATIONAL BELLAS HESS SHOULD BE OVERRULED

Overruling a constitutional precedent, while less extraordinary than overruling a statutory precedent, nevertheless requires "special justification." *Arizona v. Rumsey*, 467 U.S. 203, 213 (1984). Such justification is present when a decision of this Court not only was weakly reasoned originally but has become clearly out of step both with basic constitutional doctrine as clarified since the decision and with the present realities governed by the decision. *See Payne v. Tennessee*, 111 S. Ct. 2597, 2609-10 & n.1 (1991). In particular, in the area of state regulation or taxation of interstate business activities, this Court has frequently overruled precedents under the due process and commerce clauses to bring case law into line with coherent doctrine and current factual context. *See ibid.*; Appendix G to Brief of Amici Curiae Arizona Mail Order Company, *et al.*

Under this analysis, *National Bellas Hess, Inc. v. Department of Revenue*, 386 U.S. 753 (1967), should be overruled. It is beyond serious dispute that the imposition of use-tax collection duties on an out-of-state direct-marketing business that regularly solicits and does business within a State, like petitioner Quill, is constitutional under a straightforward application of the prevailing four-part test of *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977). Thus, as explained more fully below, such a State clearly has a substantial nexus with

sales to its residents made by a seller who has directed its sales efforts into the State and relied on state protections that make the solicitations and sales possible. The use tax is fairly related to in-state activities, since in-State users pay it; and the requirement that out-of-state sellers collect it is likewise fairly related to the state's protection of the conditions that make the commercial transaction possible, including means of communication, distribution, and disposal. There can be no problem of fair apportionment, if only because no other State can tax the use of the products within the State. *See National Geographic Soc'y v. California Bd. of Equalization*, 430 U.S. 551, 558 (1977).[1] And there is no discrimination in requiring out-of-state sellers, like their in-state competitors, to collect the use tax (or pay the coordinated sales tax).

Notwithstanding the clear validity of the tax at issue in this case under current doctrine, *National Bellas Hess* would declare the tax invalid. The reason, quite simply, is that the decision relies on doctrinal principles and factual assumptions that are not today supportable. The underpinnings of the decision, some of them inadequately considered even as an original matter, plainly are no longer valid. To the contrary, the decision undermines

[1] Nor is there a problem of duplicative taxation arising from sales taxes imposed by sellers' States. In light of constitutional problems with such a tax (*see Evco v. Jones*, 409 U.S. 91 (1972)), States have not in fact tried to impose sales taxes on their own direct marketers' sales to out-of-state customers. *See* Rothfeld, *Mail-Order Sales and State Jurisdiction to Tax*, Tax Notes at 15 n.140 (Dec. 23, 1991). In any event, any duplicative taxation problem would be fully cured by a requirement that payers of use taxes receive a credit for sales taxes paid out of State—a credit that virtually all States do provide and may even be constitutionally required. *See Williams v. Vermont*, 472 U.S. 14, 23 n.7 (1985); Rothfeld, *supra*, at 15 n.140.

central principles of commerce clause law. And there are no sufficient reasons to preserve the ruling.[2]

A. The Central Doctrinal Underpinnings of *National Bellas Hess* Have Been Clearly Repudiated by This Court.

Citing both the due process and commerce clauses, *National Bellas Hess* based its decision on the asserted validity of the "sharp distinction" between those sellers who have some physical presence in the taxing State ("retail outlets, solicitors, or property within a State") and those who do not. 386 U.S. at 758. The Court then explained that, without such presence, "it is difficult to conceive of commercial transactions more exclusively interstate in character than the mail order transactions" involved in that case. *Id.* at 759. Such transactions, the Court ruled, fall into the "domain where Congress alone has the power of regulation and control." *Id.* at 760 (footnote omitted). But both the notion that purely interstate commerce is immune from state taxation and the notion that physical presence is the essential precondition for a State to exercise authority over a person have now been clearly repudiated by this Court.

1. *The Formalist Doctrine Immunizing Purely Interstate Commerce from State Taxation Has Been Abandoned.*

The turning point of the Court's analysis in *National Bellas Hess* was its view of the mail-order transactions at issue as "exclusively interstate in character." 386 U.S. at 759. At the time that *National Bellas Hess* was decided, that characterization was important under prevail-

[2] The *stare decisis* analysis here is not altered by the fact that Congress can overturn commerce clause rulings of this Court. For one thing, *National Bellas Hess* relies on both the due process and commerce clauses (386 U.S. at 756); and it is, at a minimum, hardly clear that Congress can overturn due process rulings. In any event, this Court has in fact shown no hesitation in revising its commerce clause doctrine over the years—perhaps because Congress has been singularly inactive in resolving interstate taxing issues.

ing commerce clause doctrine. *Freeman v. Hewit*, 329 U.S. 249 (1946), and later cases such as *Spector Motor Serv., Inc. v. O'Connor*, 340 U.S. 602 (1951), had clearly established the principle, reflected in earlier decisions as well, that States could not tax "the very process of interstate commerce," so that a state tax on a purely interstate transaction, rather than on some local incident or activity, was invalid because it interfered with the freedom of interstate commerce. *Freeman*, 329 U.S. at 253. *See Trinova Corp. v. Michigan Dep't of Treasury*, 111 S. Ct. 818, 828 (1991).

This Court has, however, directly repudiated that principle since *National Bellas Hess*. In the landmark case of *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977), the Court overruled *Spector Motor* (430 U.S. at 289) and rejected "the philosophy underlying [the *Freeman*] rule" (430 U.S. at 288). Insisting on an approach to commerce clause questions based on "economic realities" (*Complete Auto*, 430 U.S. at 279), and on "the practical effect of a challenged tax" (*Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425, 443 (1980)), the Court thus explicitly abandoned what it has since aptly described as *Freeman*'s "formalistic approach" that kept certain transactions simply out of the reach of state taxing authorities. *Trinova*, 111 S. Ct. at 828. The critical doctrinal underpinning of *National Bellas Hess*, in short, is no longer good law.

2. *The Reliance on Physical Presence as the Essential Precondition to State Jurisdiction Has Been Clearly Repudiated.*

Beyond the Court's reliance on the *Freeman* principle as the *reason* for adhering to the "sharp distinction" between sellers with and sellers without physical presence in a State (386 U.S. at 758), the *National Bellas Hess* Court's very insistence on the necessity of physical presence is itself not sound. Even at the time of *National Bellas Hess*, the majority's analysis of the need for physical presence to justify exercise of taxing authority was deficient, because it ignored existing precedent on the point. Thus, the Court recognized the essential similarity of the due process and commerce clause requirements of a sufficient connection between the taxing State, its measure of taxation, and the subject of taxation. 386 U.S. at 756.[3] But the majority then wholly failed to consider the pertinent due process precedents on physical presence: *McGee v. International Life Ins. Co.*, 355 U.S. 220, 222, 223-24 (1957), had upheld a State's authority to exercise personal jurisdiction over an out-of-state firm without physical presence in the State (based on purposeful solicitation of business through mailings into the State); and *International Shoe Co. v. Washington*, 326 U.S. 310, 321 (1945), had held that the minimum contacts that were sufficient to exercise personal jurisdiction over an out-of-state company "subject[ed] it alike to taxation by the state." Together, those precedents directly undermined the *National Bellas Hess* Court's reliance on physical presence as the key to state taxing authority. Yet the Court never discussed those decisions.

In any event, since *National Bellas Hess* was decided, the Court has made crystal clear that, under the due process clause, physical presence is *not* a precondition to a State's exercise of jurisdiction over an out-of-state company. In *Burger King Corp. v. Rudzewicz*, 471 U.S. 462, 476 (1985), the Court expressly stated that physical presence is not required for personal jurisdiction, explaining that "it is an inescapable fact of modern commercial life that a substantial amount of business is transacted solely by mail and wire communications across

[3] Since *National Bellas Hess*, of course, those requirements have been stated as the nexus and fair relation components of the four-part commerce clause standard of *Complete Auto*. The Court has continued to recognize, as it did in *National Bellas Hess*, that these tests also encompass due process requirements. *See, e.g., Trinova*, 111 S. Ct. at 828; *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. at 436-37.

state lines, thus obviating the need for physical presence within a State in which business is conducted." Thus focusing on the realities of modern commerce—as the Court has done since adopting the practical, *Complete Auto* approach to commerce clause analysis—the Court in *Burger King* held that a State had jurisdiction over any business that "'purposefully directed'" its commercial efforts toward residents of the State. *Ibid.* (quoting *Keeton v. Hustler Magazine, Inc.*, 465 U.S. 770, 774-75 (1984)). There is, quite simply, no good reason why taxing jurisdiction should have to meet any higher standard than adjudicative jurisdiction, or why commerce clause standards in this regard should be any more stringent than due process standards.[4] Accordingly, the "physical presence" litmus test on which *National Bellas Hess* critically relied is not now, if it ever was, good law.

B. The Critical Factual Assumptions in *National Bellas Hess* Are Insupportable Today, Both Factually and as Grounds for Immunizing from State Tax Obligations Direct Marketers that Regularly Market in a State.

In setting forth its notions about the need for physical presence and the exclusively interstate character of the commerce at issue, the Court in *National Bellas Hess* made two critical assumptions, or assertions, of a factual nature. First, as to the State's interest, the Court indicated that a State has "no legitimate claim to impose 'a fair share of the cost of the local government'" on a seller with no physical presence in the State (386 U.S. at 760), stating earlier in the opinion that such a seller is not "accorded the protection and services of the taxing State" (*id.* at 757). Second, as to the seller's interest, the Court stressed the burden a seller would incur—and that interstate commerce would therefore incur—if the seller had to obtain and maintain accurate information about the taxes it had to collect in each of the numerous jurisdictions where it made a sale. *Id.* at 760.

[4] As to the constitutional equivalence of taxing and adjudicative jurisdiction, not only does *International Shoe* remain good law, but the equivalence follows from the fact that a State's exercise of personal jurisdiction often does mean, and constitutionally can generally mean, that an out-of-state seller is subject to the State's substantive law in the State's courts. *See, e.g., Allstate Ins. Co. v. Hague*, 449 U.S. 302 (1981); *Restatement (Second) of Conflict of Laws* §§ 6, 9, 145-146 (1971); *cf. Phillips Petroleum Co. v. Shutts*, 472 U.S. 797 (1985). This is particularly significant for direct marketers, who are forbidden by the Federal Trade Commission to bring suit against purchasers except in the courts of the purchaser's home State. *See Spiegel, Inc. v. FTC*, 540 F.2d 287 (7th Cir. 1976). *See generally* Rothfeld, *supra*, at 5-6 nn.73, 82. If a State may apply its own law in its own courts to out-of-state direct marketers, it surely can impose on those firms the duty of collecting use taxes for goods sold to in-state purchasers.

As already noted, the Court has, in its due process doctrine, repudiated the notion that a State provides no protections to businesses unless they are physically present in the State. And the *National Bellas Hess* concern with administrative burdens seems hard to wrench from the context of the majority's now-rejected focus on "exclusively interstate" commerce. But in any event, both views of the *National Bellas Hess* majority—about the absence of state protections for and the significance of burdens on out-of-state sellers—are insupportable, at least under present legal and factual circumstances.

1. *States Provide Important Protections Necessary to the Continuing, Successful Completion of Direct Marketers' Commercial Transactions.*

The majority opinion in *National Bellas Hess* essentially ignored the dissent's description of the significant protections States provide to out-of-state mail-order businesses: most notably, the States protect the soundness of the banking institutions that provide the consumer credit without which many of the transactions would be impossible; and they provide the courts that ensure collection of the purchase price from the seller's customers. 386 U.S. at 762 (Fortas, J., dissenting). Those and other protections—of the consumers who purchase, of the roads

and other means for delivering the solicitations and the goods, of the means of disposing of the inevitable waste byproducts of the seller's efforts in the State—were inadequately considered by the majority in *National Bellas Hess* and should have been sufficient to sustain the imposition of tax obligations even in 1967, even on an out-of-state seller that handled its solicitations, order-taking, and delivery entirely through the mails (or other common carrier of physical goods). But whatever the case may have been in 1967, it is clear that, today, the protections given to out-of-state direct marketers are manifold and manifestly substantial, and that States are entitled to "ask return" for those protections by demanding collection of the use tax. *See Wisconsin v. J.C. Penney Co.*, 311 U.S. 435, 444 (1940).[5]

Today, direct marketers like Quill conduct their business differently from the "mail order" business at issue in *National Bellas Hess.* Rather than relying predominantly on the mails for solicitation, direct marketers massively use the telephone and other means, such as cable television, to solicit sales. Consumers, for their part, rather than placing orders by mail, as in *National Bellas Hess* (386 U.S. at 754), now tend to place their orders by telephone (or, increasingly, by computers hooked up to telephone lines), using "800" or similar numbers that the direct marketers publish and advertise in the State. (The seller in *National Bellas Hess* had no telephone listing in the State. 386 U.S. at 754.) And rather than paying either by check or by credit arrangement directly with the seller, as in *National Bellas Hess* (386 U.S. at

[5] The seller in *National Bellas Hess* was truly a "mail order" business, in that the mails were used not only to send solicitations but to take orders for merchandise. The term "mail order" is no longer accurate for the many companies that handle their business, or a large share of it, by telephone, television, or other electronic means. Hence the more general term "direct marketer," describing companies that market goods directly to consumers, without using a retail outlet.

761 (Fortas, J., dissenting)), consumers now pay predominantly with credit cards, which are, of course, infinitely more common than they were in 1967.[6]

Given these and the other circumstances surrounding modern direct-marketing transactions, it is easy to identify the numerous protections and benefits offered by States to make the commercial transactions possible—that is, to make direct marketers' business possible. At the most basic level, States provide a host of services and protections for the economy itself—that is, for consumers' very ability to buy goods. Through schools and jobs, for example, States help create consumers with the resources to purchase. And consumers' homes and offices, where goods will be used, are protected by government fire, police, and other services. State regulation of insurance, moreover, helps protect the value of goods that consumers buy, thereby making purchase more likely.

States protect numerous aspects of the direct marketers' side of the commercial transaction as well, including solicitation, order-taking, finance, delivery, and post-purchase dispute resolution. Thus, solicitation activities that use the mails depend on roads maintained by state government, traffic regulation provided by the State, and sorting facilities protected by state police, fire, and insurance services. Solicitation activities that use electronic communication depend, for example, on the telephone network regulated by state utility commissions (and their requirements of universal service), on the telephone directories provided under state regulation, or on cable television networks regulated through local government

[6] *See, e.g.*, Stipulation in *Lands' End, Inc. v. California State Bd. of Equalization*, No. 620135 (Super. Ct., San Diego County) (86% of Lands' End sales by credit card, and 80% of orders placed by telephone).

One consequence of credit-card payment is that, even for consumers that place their orders by mail, the marketer can, upon receiving the order, calculate and add in the proper use tax to the credit card bill.

franchises. And the solicitations, when in the form of catalogs, create a major problem of waste that state governments do and must address, through garbage collection, recycling, and disposal in land fills.[7]

Beyond the solicitation, a customer's ordering of a marketer's goods depends either on the mails or on the electronic communication networks protected by the State. The seller's acceptance of the order often involves an instant credit check by the seller, conducted through the same telephone network. Payment by the customer often is made by credit card, which relies not only on the telephone network and mails for credit-checking and billing, but also on the banking system, whose soundness is a principal responsibility of state governments. Delivery of goods, once ordered and paid for, then itself depends on the roads provided by state government and on the warehouses and other facilities protected by state police, fire, insurance, and other programs. And if the commercial transaction gives rise to disputes, litigation and collection activities inevitably depend on the state courts for adjudication, sheriffs for execution, and commercial and other laws for substantive standards.[8]

[7] In fiscal year 1989, for example, Lands' End of Chicago mailed 75,000,000 catalogs averaging 156 pages each. *See Lands' End, Inc., supra.*

Paper now makes up the largest single component (40 percent) of solid waste in the country. *See* U.S. Congress, Office of Technology Assessment, *Facing America's Trash—What Next for Municipal Solid Waste*, at 73-84, OTA-0-424 (October 1989).

[8] Not only can state courts exercise personal jurisdiction over out-of-state firms that direct their business into the State (*Burger King, supra*), but an out-of-state direct marketer must, by FTC requirement, bring any suit against a customer in the customer's home-state courts (*Spiegel, Inc., supra*). A local bank providing a customer's credit card, and hence guaranteeing payment to the seller, will also use the state courts for collection efforts. And it is well-established that state consumer-protection and usury laws apply to direct-marketing transactions. *See, e.g., State ex rel. Meierhenry v. Spiegel, Inc.*, 277 N.W.2d 298 (S.D.), *appeal dismissed*, 444 U.S.

In short, it cannot seriously be contended that direct marketers who lack a physical presence in a State receive no significant protections and benefits from the States into which they protect their commercial activities. Direct marketers that sell throughout the country do not operate in a zone somehow independent of the numerous market-protecting services provided by the 50 States. To the contrary, the States provide the very infrastructure that makes the transactions of direct marketers possible.

2. *The Burdens on Direct-Market Sellers Today Cannot Justify the Rule of* National Bellas Hess.

As an initial matter, burdens on out-of-state sellers are simply not relevant to the constitutional analysis: such burdens cannot invalidate an otherwise-justified tax on (or collection duty imposed on) out-of-state direct marketers, much less support a rigid rule against such impositions unless the business is physically present in the state. Burdens on taxpayers, let alone on sellers who merely collect taxes owed by others, are simply not relevant to the "nexus" or "fair relation" tests: the former looks only to the existence of a connection between the State and the seller's activities (sale to a resident); and the latter looks only to the relation between the measure of the tax (sales price) and the in-state activities (sale in the State). *See, e.g., Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 622-26 (1981); *Exxon Corp. v. Wisconsin Dep't of Revenue*, 447 U.S. 207, 219 (1980). Neither test calls for a balancing of burdens on the seller against protections pro-

804 (1979) (consumer protection laws); *Aldens, Inc. v. Miller*, 610 F.2d 538 (8th Cir. 1979), *cert. denied*, 446 U.S. 919 (1980) (usury laws); *Aldens, Inc. v. Ryan*, 571 F.2d 1159 (10th Cir.), *cert. denied*, 439 U.S. 860 (1978) (same); *Aldens, Inc. v. LaFollette*, 552 F.2d 745 (7th Cir.), *cert. denied*, 434 U.S. 880 (1977) (same); *Aldens, Inc. v. Packel*, 524 F.2d 38 (3d Cir. 1975), *cert. denied*, 425 U.S. 943 (1976) (same). The protection of consumers by these laws, of course, gives consumers the purchasing confidence needed for direct marketers to survive.

vided by the State, whether those burdens are administrative in nature or directly monetary (such as the burden of a high tax rate). The majority in *National Bellas Hess* never explained why administrative burdens should be material to the constitutional inquiry—rather than, like the rate of the tax, simply a matter for legislative consideration. *Cf. Commonwealth Edison Co. v. Montana*, 453 U.S. at 628 (refusing to review "acceptable rate or level of taxation"). And those burdens are in fact constitutionally irrelevant. In addition to the obvious judicial unmanageability of an inquiry into "excessive" taxpayer burdens, the Court has made clear that the Constitution cannot relieve businesses of "their just share of [the] state tax burden even though it increases the cost of doing business." *Complete Auto*, 430 U.S. at 279; *see Western Live Stock v. Bureau of Revenue*, 303 U.S. 250, 254 (1938).[9]

Nor did, or could, the majority in *National Bellas Hess* explain why, even if administrative burdens were constitutionally relevant, those burdens justified a constitutional line that turns on the direct marketer's physical presence in the State. Thus, companies like Sears and Montgomery Ward may have direct-marketing divisions wholly separate from their retail outlets, and the burdens on those divisions may be identical to those incurred by direct-marketing companies with no in-state presence; yet, even before *National Bellas Hess*, it was clear that a State could freely impose those burdens on the direct-marketing parts of the businesses. *See Nelson v. Montgomery Ward & Co.*, 312 U.S. 373 (1941); *Nelson v.*

[9] Even if constitutionally relevant, the practical burdens faced by taxpayers could not justify the rigid *National Bellas Hess* rule. At most, such burdens could call for constitutional scrutiny of certain cases where state taxes imposed burdens on sellers wholly out of proportion to their in-state activities. Although even that seems intrinsically unlikely, certainly this consideration cannot justify a prohibition on a State's taxing of large companies, like Quill, that regularly solicit and conduct substantial volumes of business in the State. *See* note 11, *infra*.

Sears, Roebuck & Co., 312 U.S. 359 (1941); *see also D.H. Holmes Co. v. McNamara*, 486 U.S. 24, 33 (1988).[10] And more recently, a dozen years after *National Bellas Hess* was decided, the point became even more starkly clear. The Court held in *National Geographic Soc'y, supra*, that a minimal presence unrelated to any retail sales at all (several solicitors of advertising) was sufficient to sustain a State's requirement that an out-of-State seller (of magazines) collect use taxes—even though the administrative burden on the out-of-state part of the business was identical to what it would have been if the company had no in-state presence at all. Again, it makes no sense in light of relevant doctrine, especially as clarified since *National Bellas Hess*, to adopt a constitutional standard turning on physical presence based on concerns about administrative burdens on sellers who are exploiting the protections the State provides to their commercial transactions.

In any event, the administrative burdens on out-of-state direct marketers, however significant they were at the time of *National Bellas Hess*, are relatively insubstantial today. The burden that concerned the Court in *National Bellas Hess* was the burden of obtaining and maintaining accurate information about the taxes due in each of the jurisdictions where the seller's customers reside. But this informational burden is no longer terribly great—for precisely the same reason that has allowed direct marketing to flourish (*see* page 20, *infra*).

[10] The burden that the Court thought decisive in *National Bellas Hess* was the burden of collecting and maintaining information about the taxes in the numerous taxing jurisdictions where customers live and would use the goods sold. 386 U.S. at 759-60. It is hard to see why the constitutional inquiry should turn on whether a retail store's employees sent the information along to the separate mail-order division or, instead, the mail-order division had to write to the taxing authorities to obtain the tax information. Of course, if there were a large number of local jurisdictions with different tax requirements (a premise of *National Bellas Hess*), a company that had only a few retail outlets in a State would not likely have tax information about all those jurisdictions in any case.

Quite obviously, since 1967 there has been a revolution in information collection, processing, storage, and retrieval. Computers have become ubiquitous and cheap. It is computer technology that has allowed direct marketers to target their potential customers, to conduct mass mailings, and to handle high volumes of business. *See* M. Sroge, *Inside the Leading Mail Order Houses* at viii (3d ed. 1989). The same computer technology likewise makes possible essentially instant access to up-to-date taxing information.

Even putting aside nationwide tax manuals, the information at issue here—taxing data from some 6500 jurisdictions—is readily available in up-dated format through computer software that runs on main-frame, mini-, or IBM-type personal computers. This last type of equipment costs only several thousand dollars and is likely to be already owned and used by the direct marketer for word processing, billing, recordkeeping, and other purposes. And the software—which also prepares tax returns—costs roughly $12,000 to purchase and $10,000 per year for service and monthly updates. *See* Brief Amicus Curiae for Connecticut *et al.*, Appendix D; Brief for Respondent (fuller discussion of computer technology).

Identifying the necessary tax information is thus a task different only in degree, but not in kind, from the seller's job of identifying the shipping and handling charges for the deliveries it makes to different locations. And the task is made much simpler than the direct marketers in this case have alleged by various simplifications contained in state tax statutes. Many states have no local sales or use taxes at all; and some that do have such local taxes nevertheless provide for, or give an option of, a uniform statewide rate for out-of-state sellers. *See, e.g.*, Cal. Rev. & Tax Code § 6203(j) (West Supp. 1991); Tenn. Code Ann. § 67-6-702(f) (1989); Wash. Admin. Code, Rule 458-20-221(5) (1990). In either case a seller must keep track only of the State's own tax law, includ-

ing rates and exemptions. Keeping track of exemptions, moreover, will often be eased by the fact that such exemptions are often product-specific, so that a particular marketer may know that *all* of its goods (*e.g.*, clothing) are exempt. Finally, with respect to the burden of filing tax returns, statewide administration is now the norm: at least 40 States provide for the filing of a single tax return covering all jurisdictions within the State. *See* Brief Amicus Curiae of Direct Marketing Ass'n., Appendix 3.

In short, the costs of complying with state tax laws, if relevant at all, are not a significant impediment to the conduct of direct marketers' businesses, especially for large companies like Quill.[11] Certainly those costs are no different from the costs incurred by in-state retailers; and almost by definition, the costs are commensurate with the amount of business conducted in the State. Most fundamentally, however, these costs are nothing but the inherent price of doing business in numerous jurisdictions. When an out-of-state firm chooses to enter the market in a State, exploiting the government services that sustain the market, it may legitimately be subjected to that State's regulatory and tax laws, particularly those designed to ensure fair competition and adequate support for the government activities that make the firm's commercial transactions possible.

C. *National Bellas Hess* Directly Frustrates Vital Principles at the Heart of Commerce Clause Doctrine.

Not only is the *National Bellas Hess* rule's restriction on state taxing authority outmoded both factually and doctrinally, but it works affirmative harm to two values that are central to this Court's commerce clause jurisprudence—harm that now looms much larger than it did in

---

[11] According to Sroge, *supra*, at 445-46, Quill had sales in 1985 of $150,000,000. *See also Lands' End, Inc.*, *supra* (in 1989, Lands' End had sales of more than $500,000,000).

1967. First, the rule of *National Bellas Hess* has become a very substantial impediment to the States' ability to ensure that *all* businesses pay their fair share for the protections provided them by the State, because the rule exempts an ever-increasing portion of the Nation's sellers from *any* State's sales or use tax. Second, the rule turns the constitutional bar against discrimination on its head: it gives constitutional protection to out-of-state direct marketers against the very taxes that their in-state reail competitors may be made to pay, leaving the retailers, in fact, with an ever larger share of the state tax burden. These results are antithetical to the commerce clause notions of fairly apportioned and non-discriminatory tax burdens on commerce.

1. National Bellas Hess *Has Removed an Ever-Increasing Share of Commerce from States' Tax Base and thus Undermines States' Ability to Make All Commerce Pay Its Fair Share of Government Services.*

The magnitude of the *National Bellas Hess* rule's impact on the States has dramatically increased since 1967. In 1967, total mail-order sales were estimated at \$2.4 billion. *National Bellas Hess*, 386 U.S. at 763 (Fortas, J., dissenting). By 1989, direct-marketing sales were estimated at \$183.3 billion. Pet App. A12; *see also* Hartman, *Collection of the Use Tax on Out-of-State Mail-Order Sales*, 39 Vand. L. Rev. 993, 1006 (1986) (50 to 150 billion dollars in 1985). These figures reflect the fact that direct-marketing sales have grown faster than local retail sales, thus taking over an ever larger share of total sales. *See* Sroge, *supra*, at ix; H. Bruce, *Industry Outlook: What Happens Next?*, DM News (June 18, 1990), at 13 (between 1980 and 1989, direct-marketing sales grew at 15% a year, while retail sales grew at 5% a year). Today, direct marketing sales account for between 15 and 25 percent of all retail sales in this country. Hartman, *supra*, at 1007-08.

The consequence of these developments, under the rule of *National Bellas Hess*, is that States are being stripped of an ever larger part of their tax base. More and more of the sales business of the United States—not subject to use taxes in the customers' States and not subject to sales taxes in the sellers' States—is becoming immune from taxation, as though it were part of the national economy without being part of any State's economy. The loss in revenues to financially strapped States was estimated at \$1 billion in 1985 and \$2 billion in 1988. *See* Hartman, *supra*, at 1007-08; Advisory Comm'n on Intergovernmental Relations (ACIR), *Estimates of Revenue Potential from State Taxation of Out-of-State Mail Order Sales* at 8 (Staff Information Report SR-5, Sept. 4, 1987). Yet sales and use taxes have become an increasingly important revenue source since 1967, rising from 19% of total state tax revenues in 1967 to 24% in 1982, with most States having raised their rates. *See* ACIR, *State and Local Taxation of Out-of-State Mail Order Sales* at 6 (Commission Report A-105, Apr. 1986); Rothfeld, *supra*, at 5-6 & n.16.[12]

In addition to being a matter of great practical concern to the States, this removal of an increasingly substantial part of commerce from States' revenue base is of constitutional concern. Central to its modern commerce clause jurisprudence, the Court "consistently has indicated that 'interstate commerce may be made to pay its way.'" *Complete Auto*, 430 U.S. at 281. That principle not only acts as a limit on commerce clause restrictions imposed on the States; it is itself an affirmative, constitutionally rooted protection of the States, implicit in the constitutional structure's commitment to a federal system that protects traditional state power like the power to tax those who exploit state protections. *See Boston Stock*

[12] According to the cited 1986 ACIR report (at 24-25), in 1983, sales tax revenues provided between 16 and 59 percent of individual state tax revenues.

Exch. v. State Tax Comm'n, 429 U.S. 318, 328-29 (1977) ("reserved 'power of the States to tax'") (quoting *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1, 199 (1824)). *National Bellas Hess* has become a serious practical threat to that cardinal principle.

2. National Bellas Hess *Sanctions Discrimination Between In-State Businesses and Their Out-of-State Competitors.*

At the same time that it threatens the important interests of the States, *National Bellas Hess* also works immediate harm to the in-state retail competitors of out-of-state direct marketers. That harm is of two kinds. First, in-state retailers are placed at a direct disadvantage in competing for customers against out-of-state direct marketers, because under *National Bellas Hess* the out-of-state sellers need not charge to their customers the very taxes that their in-state competitors must charge to their customers. When tax rates are roughly 5-8%, that differential provides a substantial benefit to the out-of-state company. Second, when the out-of-state marketers are removed from a State's tax base, in-state businesses must pay even higher taxes to make up for the revenue shortfall to the State. This shifting of an increased burden onto the in-state businesses further accentuates the advantage given out-of-state marketers by *National Bellas Hess*.

A rule commanding such favoritism turns the antidiscrimination principle of the commerce clause upside down. That principle is designed to "maintain state boundaries as a neutral factor in economic decisionmaking." *American Trucking Ass'ns, Inc. v. Scheiner*, 483 U.S. 266, 283 (1987); *see Boston Stock Exch. v. State Tax Comm'n*, 429 U.S. at 329-33. Yet the rule of *National Bellas Hess* gives a distinct advantage to a business depending on whether it is located outside or inside a State, thus affirmatively encouraging a retailer to close up shop,

move out of State, and sell its goods as a direct marketer. That is the antithesis of ensuring the neutrality of state boundaries.

By contrast, the extension of use tax collection duties to out-of-state direct marketers directly serves the commerce clause goal of equal treatment of all commercial competitors, whether in-state or out-of-state. Such an extension serves not only "to compensate the state for revenue lost when residents purchase out-of-state goods for use within the State" (*D.H. Holmes Co.*, 486 U.S. at 32), and thus to force out-of-state marketers that exploit in-state customers to share some of the revenue burden carried by their in-state retail competitors; it also serves the fair-competition purpose of removing a substantial inequality in the terms on which they compete for customers. So, too, the overruling of *National Bellas Hess* would promote the constitutional goal of equal treatment of interstate and intrastate commerce.

D. Reliance Interests and Concerns About Line-Drawing and Retroactivity Do Not Justify Leaving *National Bellas Hess* in Place.

Retention of *National Bellas Hess* has been urged on the ground that out-of-state direct marketers have relied on the rule. Another reason given for retaining the rule of *National Bellas Hess* is that some direct marketers may have difficulty determining whether they meet the various States' tests of "regularly" or "systematically" soliciting business in the State. And concerns about the potential disruption caused by the potential retroactivity of an overruling of *National Bellas Hess* have also been advanced as a reason not to overrule the decision. None of those arguments can justify leaving this rigid, erroneous, unfair, and outmoded decision on the books.

1. *Reliance.* The asserted reliance interests cannot warrant retention of *National Bellas Hess.* To begin with, the claimed reliance interests are no different from those

present in the several other cases in which this Court has nevertheless overruled commerce clause precedent to eliminate artificial, outmoded doctrinal limitations on taxing authority. *See, e.g., Goldberg v. Sweet*, 488 U.S. 252, 265 n.16 (1989); *Commonwealth Edison Co. v. Montana, supra*; *Department of Revenue v. Association of Washington Stevedoring Cos.*, 435 U.S. 734 (1978); *Complete Auto, supra.* And this process of doctrinal evolution, especially in the commerce clause area, has long been a familiar and expected part of the constitutional regime under which commercial enterprises must make their business decisions. *See Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 473 (1959) (Frankfurter, J., dissenting).

The reliance interests are particularly weak in this case. The *National Bellas Hess* rule has been subject to serious question in prominent scholarly literature for many years, and it has been clear at least since *Complete Auto* that the central doctrinal underpinning of the decision is no longer good law. *See, e.g.*, Hartman, *supra*; P. Hartman, *Federal Limits on State and Local Taxation* § 10:8, at 627-28 (1981). Moreover, investments made in reliance on blatantly discriminatory favoritism are hardly worthy of special regard. Direct marketers who grew dramatically faster than their in-state retail competitors based on such advantages over the past 20 years should not now be heard to complain that they must at long last compete on more equal terms. And that, of course, is the only result of overruling *National Bellas Hess*, which would hardly stop direct marketers from engaging in their businesses. The complaints about impaired reliance interests have a peculiarly hollow ring when all that is being done is to force direct marketers to share a tax-collection burden that their competitors already incur. In any event, these complaints are insufficient to stand in the way of correcting an anomalous precedent that is profoundly unfair to both the States and in-state businesses.

2. *Line-Drawing.* Retention of *National Bellas Hess* likewise cannot be justified on the ground that there is no bright line between those direct marketers who do, and those who do not, meet state statutory or constitutional nexus standards. For one thing, the line-drawing problems, which are initially a question of notice to direct marketers and secondarily a question of judicial definition of the line, are substantially exaggerated by the direct marketers in this Court. Some States, like North Dakota in this case, provide an easy-to-apply rule: in the present case, three separate advertisement mailings in a year. Pet. App. A56. Moreover, state taxing authorities are available and likely to provide guidance to marketers, by regulation or otherwise.

Even aside from such aids to application, however, the standard itself—certainly the constitutional minimum of purposeful in-state solicitation, but also the prevalent statutory criteria, *see* Brief Amicus Curiae of National Conference of State Legislatures *et al.* on Petition for Writ of Certiorari at 7-8 & nn.6 & 7—should not present any substantial practical problems. The fact is that even a standard of regular, substantial, systematic, or recurring directed marketing into a State is sufficiently low, indeed not materially different from a simple purposeful solicitation standard, that virtually all direct marketers who deliberately direct their selling activities into a State will have to, and know that they have to, comply with their use-tax collection duties. These standards are, quite simply, every bit as manageable as the purposeful availment standard for due process analysis of personal jurisdiction. *See Burger King, supra*; *McGee, supra.*

In any event, these concerns about practical problems in marginal cases cannot conceivably justify retention of the rigid rule of *National Bellas Hess.* That rule immunizes even large companies doing substantial volumes of business in a State from the tax obligations shouldered by their in-state competitors. That result is so clearly

wrong that it should be overruled even if, at a later time, state courts or this Court might have to address whether a particular low level of activity directed into the State is insufficient under state statutes or the Constitution. Just as in *Complete Auto*, "administrative convenience, in this instance, is insufficient justification for abandoning the principle that 'interstate commerce may be made to pay its way.'" 430 U.S. at 288 n.15.

3. *Retroactivity*. Finally, concerns about the retroactivity of a decision overruling *National Bellas Hess* cannot justify retaining the decision. It is sufficient to say that the question of retroactivity is separate and distinct from the question of the continuing validity of the *National Bellas Hess* rule. The retroactivity question presents an issue for another day in another case.

CONCLUSION

National Bellas Hess should be overruled, and the judgment of the Supreme Court of North Dakota should be affirmed.

Respectfully submitted,

ROBERT J. DEL TUFO
Attorney General of New Jersey
SARAH T. DARROW *
Deputy Attorney General
JOSEPH L. WANNOTTI
Assistant Attorney General
R.J. Hughes Justice Complex
C.N. 112
Trenton, NJ 08625
(609) 633-8455

RICHARD G. TARANTO
JOEL I. KLEIN
KLEIN, FARR, SMITH & TARANTO
2550 M Street, N.W.
Washington, D.C. 20037
(202) 775-0184

* *Counsel of Record*

Dated: December 26, 1991